(3)

No. 87-1685

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

SHELL OIL COMPANY,
Petitioner,

vs.

CITY OF SANTA MONICA,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

BRIEF AMICUS CURIAE OF THE WESTERN OIL AND GAS ASSOCIATION, et al., IN SUPPORT OF PETITIONER

(Additional Amici Listed on Back of Front Cover)

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(Additional Amici)

Amoco Production Company

Atlantic Richfield Company

Chevron U.S.A. Inc.

Conoco Inc.

Edgington Oil Company, Inc.

Mobil Oil Corporation

Phillips Petroleum Company

Texaco Inc.

Union Pacific Resources Company

Unocal Corporation

QUESTION PRESENTED

The core issue presented by this case is whether a municipality can, consistent with the Commerce Clause, charge a fee to an interstate pipeline operator for the right to pass beneath its streets that has no relation to costs incurred by the municipality or the value of the property involved.

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BRIEF AMICUS CURIAE OF THE WESTERN OIL AND GAS ASSOCIATION, et al., IN SUPPORT OF PETITIONER[1]

INTEREST OF AMICI CURIAE

Amici Amoco Production Company, Atlantic Richfield Company, Chevron U.S.A. Inc., Conoco Inc., Edgington Oil Company, Inc., Mobil Oil Corporation, Phillips Petroleum Company, Texaco Inc., Union Pacific Resources Company and Unocal Corporation are companies that either directly or through subsidiary corporations operate

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[1] Consent letters from the parties have been filed with the Clerk.

petroleum pipelines throughout the nation. Amicus Western Oil and Gas Association is a regional trade association representing companies and individuals that conduct much of the producing, refining, transporting and marketing of petroleum in the western United States. Amici petroleum companies are members of the association. Of necessity, such companies transport large volumes of crude oil and refined petroleum products in interstate commerce through urbanized areas where the pipelines must run beneath city streets.

Historically, such subsurface corridors have been treated as an extension of the street, useful only for public transportation purposes and therefore of essentially no commercial utility. Accordingly, only a moderate fee, consistent with the greatly reduced value of property already encumbered with a street easement (and which often does little more than recover municipal administrative costs), has been charged for the right to pass. The respondent in this case, City of Santa Monica, seeks to alter that historical practice and charge for the use of land beneath its streets in accordance with the commercial value of abutting private property. This results in a fee which, in this instance, is more than 23 times higher than would result from application of a more traditional formula. If adopted by other municipalities, such an approach could have profound effects on the cost of operating petroleum pipelines and the bulk liquid transportation business.

REASONS FOR GRANTING THE WRIT

I.

SUMMARY OF ARGUMENT

The fee involved in this case would be imposed by respondent in its capacity as a trustee for the rights held by the public in city streets, rights which exist for the sole purpose of facilitating travel and commerce. Respondent is therefore acting as a market regulator rather than a participant in the market and the dormant Commerce Clause imposes a limitation on what it can charge. Because the fee is being exacted for the use of property controlled by the government in its sovereign capacity, it is to be analyzed by the courts as a "user fee."

The test this Court has repeatedly affirmed as the proper gauge for whether a user fee is excessive and therefore an unreasonable burden on commerce is whether it is a fair approximation of the *cost* to local government of providing the facility or service involved. The Ninth Circuit's conclusion that a fee based on abutting private property values satisfies this test is erroneous and in conflict with decisions of this Court. Unlike abutting property, respondent has paid nothing to acquire the street easement, including any subsurface rights, and the municipality provides no other service and incurs no other cost (other than the cost of administering the franchise) for which compensation would be appropriate.

Even if another test which has sometimes been articulated by this Court — whether the fee approximates the *value* of the facility being provided — is applied, the Ninth Circuit's conclusion is still incorrect. The value of land is a reflection of its usefulness for other purposes or by other persons. Alternative uses or users for land beneath

city streets are extremely limited due to the burden placed on the surface estate by its dedication to street purposes. Nor is there any relationship between abutting real estate prices and the value of land beneath the street. Pipeline operators using transportation corridors beneath city streets are not like tenants leasing easements through private property, which decrease the commercial value of surface use. The purpose to which transportation corridors are put, the movement of persons and goods, involves a nonexclusive use which pipeline operators enjoy in common with other members of the public. That use is not enhanced or made more valuable by the price of abutting property.

The Ninth Circuit's error appears to result from a misapplication of its own decision in an earlier case (*Western Oil and Gas Association v. Cory*, 726 F.2d 1340 (9th Cir. 1984), *aff'd per curiam by an equally divided Court*, 471 U.S. 81 (1985)), which found that fees for pipeline easements across state-owned tidal and submerged lands based on the volume of petroleum being shipped violated the Commerce Clause but indicated in dicta that, where the easements impact upon surface use for commercial purposes, such fees can be based on the appraised value of the specific land involved (*not* abutting property values).

The petition should be granted to review this error by the Ninth Circuit and correct it before the mistake is proliferated by the thousands of other municipalities and local governmental jurisdictions across the country through which interstate pipelines must pass.

II.

REVIEW IS NECESSARY TO CORRECT AN INTERPRETATION OF THE COMMERCE CLAUSE WHICH COULD RESULT IN EXORBITANT FEES FOR THE RIGHT TO TRANSPORT GOODS BY PIPELINE THROUGH URBANIZED AREAS

A. Interstate Petroleum Pipelines Must Frequently Traverse Urbanized Areas Where There Is No Alternative To Crossing Or Running Under City Streets

It has recently been estimated by the Department of Transportation that there are over 113,000 miles of interstate liquid pipelines in the United States. In 1986, almost 3 1/2 trillion barrel miles of liquid were shipped through this interstate pipeline network, a volume of trade equivalent to 19 billion miles of surface travel by tank trucks. Most of these shipments involve crude oil or refined petroleum products. As a result, 40% of the nation's annual supply of energy moves through inter and intrastate pipelines.[2]

A significant part of the interstate pipeline system is located in urbanized areas where it is not possible to avoid crossing under the grid of city streets or, if an area is already substantially built-up, along and under the street corridor itself. To illustrate this point, in 1987, the City of

[2] Pipelines have proven to be an extremely safe way to transport these large volumes of liquid. According to the National Transportation Safety Board, pipeline shipments result in by far the fewest fatalities per billion ton-miles of cargo shipped in the United States of any transportation mode.

Los Angeles reported that there were over 500 miles of bulk liquid pipelines located beneath its streets, many if not most of which were transporting crude oil or petroleum products moving in interstate commerce. In highly urbanized areas like Los Angeles, there is no place to put pipelines other than under the streets and pipeline operators must pay whatever fee the municipality demands.

B. A Fee For The Right To Pass Based On The Price Of Real Estate Abutting City Streets Could Have Profound Effects On Pipeline Operating Costs and Transportation Decisions

As in this case, municipalities typically do not own the land beneath their streets. *Shell Oil Co. v. City of Santa Monica*, 830 F.2d 1052, 1054 (1987). They only have an easement, usually exacted from adjoining property owners in exchange for the right to develop their property, to use the surface for street purposes. This has generally been interpreted to include a sufficient amount of land beneath the surface to support street use. *Kane v. City of Chicago*, 384 Ill. 361, 57 N.E.2d 523 (1943), *rev'd on other grounds*, 392 Ill. 172, 64 N.E.2d 506 (1945); *1426 Woodward Ave. Corp. v. Wolff*, 312 Mich. 352, 20 N.W.2d 217 (1945); *Harrison County v. City of Marshall*, 253 S.W.2d 67 (Tex. Civ. App. 1952). However, as noted by one eminent authority, "[w]hatever may be the quality or quantity of the estate of the city in its streets, that estate is essentially public and not private property, and the city in holding it is considered the agent and trustee of the public and not a private owner for profit or emolument." E. McQuillin, *The Law of Municipal Corporations*, Vol. 10, 685 (3rd Ed. 1981). Furthermore, "the streets and public ways of a municipal corporation are held by it in trust for the public,

to be used for the ordinary purposes of travel and such other uses as customarily pertain thereto which, in recent years, are numerous and various." *Id.* at 762.

Use of land beneath city streets to construct and operate petroleum pipelines is a proper use. The authority to regulate streets exercised by municipalities is delegated from the state and, in California as well as many other states, the propriety of using land under public streets for pipelines is expressly confirmed by statute. *See, e.g.*, Cal. Pub. Util. Code §6202 (Deering 1970); Mich. Comp. Laws Ann. §22-1341, §22-1581 *et. seq.* (West 1988); N.J. Stat. Ann. §40-67-1 (West 1967); Tex. Rev. Civ. Stat. art. 1082 (Vernon 1963). For example, §6202 of the California Public Utilities Code expressly authorizes the legislative body of any municipality in California to grant limited rights, known as franchises, to construct and operate petroleum pipelines under its streets.

Pipeline franchises are typically limited in duration, nonexclusive, relocatable at the municipality's request, and convey no property rights in the land beneath the streets through which they pass. In actuality, they are only a license to temporarily occupy a specified amount of subsurface space.[3] Because of the tenuous nature of the rights conferred, the lack of other beneficial uses for land located immediately beneath streets, the fact that the corridors involved are dedicated exclusively to the facilitation of travel and commerce, and the significant transportation burden underground pipelines remove from surface use, such franchise rights have historically been

[3] Such temporary occupancy is necessary because of the need to physically contain bulk liquids while they are being transported. Like goods moving by truck on the surface of the street, the commodity actually being shipped is simply passing through and only occupies the subsurface space for an extremely brief period of time.

accorded a relatively modest value. Consistent with the limited value ascribed to land already burdened with a street easement, any fee imposed for the use of the subsurface corridor has usually been set at a level which does little more than attempt to recover the cost to the municipality of administering the franchise.

Typical annual pipeline franchise fees in Southern California, for example, have been set at between 1/2 cent and 2 cents per diameter inch per lineal foot of line. For general law cities in California, the annual rate for non-public utility crude oil and product pipelines is set by statute at 1/2 cent per inch per foot unless some other amount or formula is agreed upon by the operator and the municipality. *See* Cal. Pub. Util. Code §6231 (Deering 1970). It was the decision by respondent, a charter city not bound by §6231 of the Public Utilities Code, to substantially change the basis on which the annual franchise fee is calculated for the only crude oil pipeline passing through its jurisdiction that led to this litigation. Respondent proposes to charge for the land occupied by the pipeline at rates commensurate with those obtainable by an abutting private property owner if it were to lease an easement through its property which impinged upon surface commercial use.

This philosophical difference in the way land beneath city streets is to be viewed results in a strikingly different annual charge to the pipeline operator. In the case of petitioner, the difference is between $10,000, the amount its appraiser estimates Shell Oil Company would have to pay for its 10 inch diameter 3.9 mile pipeline segment under a traditional franchise fee formula, and $237,000, the fee derived by respondent based on abutting real estate values in the City of Santa Monica. *See* 830 F.2d at 1054-55. Such a shift in the way subsurface land in city streets is valued (in this case, resulting in a fee more than 23 times higher than would result from application of a more traditional formula), if

widely endorsed by other municipalities, could have profound consequences for petroleum transportation economics and affect future decisions concerning the method to be used to transport crude oil and refined products.

C. A Fee Imposed On An Interstate Pipeline For The Right To Cross Or Run Under City Streets Is Subject To Commerce Clause Scrutiny As A "User Fee"

It was established long ago that the control exercised by local government over transportation corridors, when it impacts upon interstate pipelines, is subject to Commerce Clause scrutiny. *See West v. Kansas Natural Gas Co.*, 221 U.S. 229 (1911). Given that respondent's only claim to authority over city streets is as a trustee for the public and to assure free passage, there would seem to be little question that respondent is acting as a market regulator rather than a participant.

Similarly, because the fee involved is being imposed for the use of property controlled by the government in its sovereign capacity and because it is axiomatic that the practical effect of an exaction, not its label, is to be the focus of any analysis under the Commerce Clause, *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), *Lawrence v. State Tax Commission of State of Mississippi*, 286 U.S. 276, 280 (1932), this case falls squarely within the bounds of the Supreme Court cases addressing the propriety of so-called "user fees." In this regard, we would note that the Ninth Circuit, both here and in its earlier decision in *Western Oil and Gas Association v. Cory*, 726 F.2d 1340 (1984), *aff'd per curiam by an equally divided Court*, 471 U.S. 81 (1985), heavily relied upon by the Ninth Circuit in this case, concluded that a user fee analysis was required.

We do not contest this portion of the Ninth Circuit's decision. We believe it is correct. It is the way in which the Circuit Court performed the analysis that is problematic.

D. A Fee For The Right To Pass Under City Streets Based On The Price Of Abutting Real Estate Does Not Represent A Fair Approximation Of Local Government Costs

As this Court recently reaffirmed in *American Trucking Associations v. Scheiner*, 483 U.S. ___ , 107 S.Ct. 2829, 2843-44 (1987), the principles announced in *Evansville-Vanderburgh Airport Authority District v. Delta Airlines, Inc.*, 405 U.S. 707 (1972), remain the guiding light in the area of permissible user fees. In addition to confirming that "it is the amount of the tax [or user fee], not its formula that is of central concern" and that the fee must not be "excessive in comparison with the governmental benefit conferred," the broad overriding principle that emerges from *Evansville-Vanderburgh* is that local governments may levy fees designed to help defray the cost of providing facilities or services but such charges cannot be "excessive in relation to costs incurred by the taxing authorities." 405 U.S. at 719. If they are, the user fee does not pass Constitutional muster.

In stating this test, *Evansville-Vanderburgh* builds upon a long history of decisions in which the Court has repeatedly articulated the proposition that the proper function of a user fee is to recover for the governmental entity imposing the fee what is a fair and reasonable contribution toward the cost of constructing and maintaining the public facility or providing the service involved. *See e.g., Hendrick v. Maryland*, 235 U.S. 610 (1915) (upholding registration and license fees imposed for, among other purposes, "to secure some compensation for the use of facilities provided at great

cost from the class for whose needs they are essential, and whose operations over them are particularly injurious"); and *Sprout v. City of South Bend, Indiana,* 277 U.S. 163 (1928) (disapproving a municipal registration and licensing ordinance, but reaffirming that "a state may impose, even on vehicles engaged exclusively in interstate commerce, a reasonable charge as their fair contribution to the cost of constructing and maintaining the public highways"). *Accord, Commonwealth Edison Co. v. Montana,* 453 U.S. 609, 622 n.12 (1981).

While aware of the guidance provided by *Evansville-Vanderburgh* and the cases upon which it built, the analysis performed by the Ninth Circuit in this case makes no attempt to assess whether the fee respondent proposes to impose upon petitioner for the right to pass beneath its streets represents a fair approximation of the cost to the City of providing such right. It also overlooks the fact that, given the magnitude of the fee being imposed, the only possible purpose of the exaction is general revenue generation, not cost recovery.

Unlike the abutting properties to which respondent attempts to tie the fee, the City acquired the street easements and the land beneath them at no cost to itself or its taxpayers. Because all pipeline construction expenditures, maintenance expenses and the cost of any harm inflicted upon the street surface by the line's existence must either be paid directly by the pipeline operator or reimbursed to the City, there is no other service or cost incurred by respondent for which compensation can be imposed without running afoul of Commerce Clause constraints. Although acknowledging the user fee test set forth in *Evansville-Vanderburgh,* the Ninth Circuit has simply failed to perform the required analysis.

E. A Fee For The Right To Pass Under City Streets Based On The Price Of Abutting Real Estate Does Not Approximate The Value Of The Subsurface Corridor Being Provided

Another expression of the user fee test which has been articulated in some of the cases is whether the fee imposed approximates the value of the facility or service being provided. *See, e.g., American Trucking Associations v. Scheiner,* 107 S.Ct. at 2844 ("cost or value of"). This yardstick may be a limitation on the cost recovery test reaffirmed in *Evansville-Vanderburgh* (limiting cost recovery to the value of the facility or service provided) or simply a restatement of the same test using different words (expressing the thought that cost and value are roughly equal). Its exact role is unclear.

If it is an independent test for Commerce Clause validity, it has not been met in this case. The land beneath city streets is of no commercial value to a municipality because the only rights it has in the property are for the purpose of facilitating public transit and trade. A city is not at liberty to rent or lease such rights for profit. *McQuillin, supra* at 685.[4] Since any subsurface rights that are acquired as part of the street easement are for the same purpose, such rights are

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[4] In those cases where a municipality grants an *exclusive* franchise to a public utility to run lines beneath its streets — for distribution of natural gas or electricity, for example — it is customary to impose a fee based on a percentage of the utility's gross receipts. *See, e.g.*, Cal. Pub. Util. Code §6231 (Deering 1970). Such a situation, in which the municipality may make a profit, is quite different from the granting of a *non-exclusive* franchise to a petroleum pipeline operator. Exclusive public utility distribution franchises confer a monopoly right to serve residents of the community and the fee exacted from the utility is for that privilege, not for the right to pass through.

also of no commercial value and cannot be used to generate general revenue. The only use to which the subsurface can be put by the municipality is to reduce the burden on surface traffic by allowing some of it to move below ground. That is, of course, the major benefit to a city of granting pipeline franchises — the surface is thereby freed up for other travel and transportation purposes.

If viewed instead from the perspective of the pipeline operator, there is still no correlation with abutting real estate prices. Since the value of land is determined by what it will bring in the market and that is determined by the existence of alternative uses or users who are at least theoretical competitors for the right to use the property, there is a vast difference between the value of real estate abutting a city street and the value of the street itself. Because of the infinitely greater number of uses to which the private property can be put, it is not comparable to land beneath city streets already burdened with a transportation easement. In fact, the subsurface corridor is so burdened by the surface use that it is valueless for anything but transportation (or transmission) purposes.

Nor are abutting real estate prices of even tangential relevance to the pipeline operator. The decision to use the subsurface corridor is not dictated by the operator's ability to generate rents or obtain other unique benefits due to location (what usually influences real estate values) but rather by the same considerations that motivate use of the street surface, the utility of the corridor in transporting goods from one location to another. Whether the abutting real estate is high priced and can therefore support higher rents or is of no commercial worth is irrelevant to the pipeline operator. It has no bearing on the value he places on the right-of-way beneath the street.

Consequently, whether "value" is assessed from the municipality's perspective or that of the pipeline operator,

the conclusion is the same. The price of real estate abutting the street is irrelevant to the value of the subsurface transportation corridor.

F. The Ninth Circuit's Error Appears To Result From A Misapplication Of Its Own Earlier Decision In *Western Oil And Gas Association v. Cory*

Western Oil and Gas Association v. Cory, 726 F.2d 1340 (9th Cir. 1984), *aff'd per curiam by an equally divided Court*, 471 U.S. 81 (1985), involved a challenge by certain of the amici on this brief to rental charges imposed for the use of state-owned tidelands and submerged lands which were tied to the volume of petroleum passing over the leased property. The Ninth Circuit concluded that such a "throughput charge" was not designed to compensate the state for the use of its land and that no other services or facilities were being provided for which compensation could be exacted. *Id.* at 1344. Accordingly, it determined that the throughput charge did not satisfy the *Evansville-Vanderburgh* user fee test and violated the Commerce Clause. *Id.*

In reaching its decision, the Ninth Circuit observed that the state had used a different type of leasing system before the throughput charge was enacted, a system under which rentals were based on the appraised value of the land being used (not abutting property). While the earlier system was not challenged in *Cory* and therefore was not before the Court for review, the Ninth Circuit noted by way of dicta that "California does have the right to exact compensation for conferring upon plaintiffs the right to use the real estate in question." 726 F.2d at 1344. However, it did not pass on the propriety of the specific appraisal-based rental fees

which had been imposed prior to adoption of the throughput charge.

In addition to the obvious difference between lands held in fee by the state which have commercial value and the street easements possessed by respondent in this case, the reason plaintiffs did not challenge the appraisal-based fees discussed in *Cory* becomes more apparent when an earlier state court decision in the same litigation is examined. *See Western Oil and Gas Association v. California State Lands Commission,* 105 Cal.App.3d 554, 164 Cal.Rptr. 468 (1980). That decision makes clear that the appraisal-based fees were only intended to apply to commercial and industrial sites involving surface use or which precluded rental of the surface to others for commercial purposes. 105 Cal.App.3d at 558, 164 Cal.Rptr. at 470. Consistent with historical valuation practices for subsurface pipeline corridors where surface use is not impacted (such as under a city street), the state's schedule provided for rental of pipeline rights-of-way at the rate of 1 cent per diameter inch per lineal foot. *Id. See also* Cal. Admin. Code tit. 2 §2005(b)(6) (1970).[5]

Because the Ninth Circuit apparently misunderstood the appraisal-based rental charges discussed in *Cory* and incorrectly concluded that the case had endorsed a commercial real estate value-based fee for pipeline rights-of-way under circumstances similar to those existing in this case, it failed to perform the rigorous Commerce Clause analysis mandated by *Evansville-Vanderburgh* and other

[5] The state court decision also notes that rents for pipeline rights-of-way were increased to 1 1/2 cents per inch per foot at the time the unlawful throughput charge was adopted, thereby allowing the state to use whichever formula provided the most revenue. 105 Cal.App.3d at 559, 164 Cal.Rptr. at 470. *See also* Cal. Admin. Notice Reg. tit. 2 §2006(b)(8), Reg. 75, No. 15-Z, p.6 (1975).

decisions of this Court.[6] It should have performed that analysis and concluded that a pipeline franchise fee based on abutting property values does not result in a fair approximation of the costs being incurred or services being provided by respondent and, to the contrary, is designed solely to generate substantial general revenues for the City of Santa Monica in violation of the Commerce Clause.

CONCLUSION

For the foregoing reasons, amici respectfully urge the Court to grant the petition and correct the error committed by the Ninth Circuit before it is emulated by other jurisdictions and becomes the standard method of charging for pipeline franchise privileges throughout the United States.

DATED: May 2, 1988

Respectfully submitted,

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[6] As pointed out by petitioner in its brief in support of the petition, in reaching its decision, the Ninth Circuit also incorrectly concluded that the district court had decided an issue of fact, the fair market value of the subsurface right-of- way, which had never been presented to the trial court, and then proceeded to improperly affirm that finding. Petition for Writ of Certiorari at 11, *see* n.6 and accompanying text.